

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

APPLICATION OF BIG SANDY)	
WATER WORKS, INC., FOR AN)	
ADJUSTMENT OF RATES PURSUANT)	CASE NO. 8631
TO THE ALTERNATIVE PROCEDURE)	
FOR SMALL UTILITIES)	

O R D E R

On August 26, 1982, Big Sandy Water Works, Inc., ("Big Sandy") filed an application with the Commission to increase its water rates pursuant to 807 KAR 5:076. This regulation allows utilities with 400 or fewer customers or \$200,000 or less gross annual revenues to use the alternative rate filing method ("ARF") in order to minimize the necessity for formal hearings, to reduce filing requirements, and to shorten the time between the application and the Commission's final Order. This procedure minimizes rate case expenses to the utility and, therefore, results in lower rates to the ratepayers.

Big Sandy requested rates which would produce an annual increase of \$32,718. According to Big Sandy's application, this increase is necessary to maintain the quality of water and service to its customers, to install new lines, and replace service connections and meters. In this Order the Commission has denied an increase in rates.

There were no intervenors in this matter, and no protests were entered. All information requested by the Commission has been submitted.

TEST PERIOD

For the purpose of determining the reasonableness of the proposed rates, the 12-month period ending December 31, 1981, has been accepted as the test period.

REVENUES AND EXPENSES

Operating Revenues

Big Sandy has few formal records of its operations, and the records that it does have are not traceable to source documents nor maintained in accordance with the Uniform System of Accounts as prescribed by the Commission. It is impossible to reconcile the amount of revenue reported by Big Sandy on its income statement of \$57,070, and the amount of revenue derived from its billing analysis for the same period of \$75,975, due to faulty collection practices, poor bookkeeping, and lack of proper accounting procedures. Therefore, the Commission has adjusted Big Sandy's operating revenue by \$18,905 to agree with the billing analysis.

In an attempt to reconcile the revenue figures cited above, members of the Commission staff conducted a billing audit at

Big Sandy's premises on November 18, 1982.⁽¹⁾ During the investigation it was disclosed that free service is provided to two residential customers, a rate different than the rate prescribed by the existing tariff is charged to two grocery stores, free service is granted to 10 owners of swimming pools, and some customers are granted water service in exchange for services. Based upon Big Sandy's tariffed rates and Commission regulations these practices are not proper, constitute discrimination and are, therefore, illegal and must cease upon application of KRS 278.160 and 278.170. In addition, Big Sandy often reduces bills on complaint by customers without verification that the billing is incorrect. It was also later disclosed that revenues received from two rental properties located on Big Sandy's premises are not recorded. This practice must also cease and revenues received from the rental properties should be recorded as other income on Big Sandy's books.

The Commission advises Big Sandy to correct its deficiencies in recordkeeping, billing, and revenue collections. Furthermore, the Commission is of the opinion that if it corrects the above-stated deficiencies, Big Sandy should have sufficient revenues.

Operating Expenses

In order to reflect current operating conditions, Big Sandy proposed average expenses and average billings without sufficient documentation to support known and measurable increases

(1)

Report on Investigation of Records and Billing Procedures of Big Sandy Water Works, Inc., For Case No. 8631.

in expenses, with the exception of the electric expense, which the Commission has increased by \$670.

The Commission advises Big Sandy that prior to filing future rate cases, it should familiarize itself with the Commission's policy concerning pro forma adjustments.

The Commission finds that Big Sandy's adjusted test period operations are as follows:

	<u>Actual</u>	<u>Adjustments</u>	<u>Adjusted</u>
Operating Revenues	\$57,070	\$18,905	\$75,975
Operating Expenses	50,834	670	51,504
Net Operating Income	<u>\$ 6,236</u>	<u>\$18,235</u>	<u>\$24,471</u>

REVENUE REQUIREMENTS

The determination of the revenue requirement in a privately-owned company is based on a valuation of net investment in utility operations and capital supporting that investment. A fair rate of return on that investment is determined and applied to the net investment valuation. The fair rate of return on net investment is determined as the reasonable cost of equity to the stockholders of the company plus interest on debt. However, in this case, this method of revenue requirement determination is not appropriate since Big Sandy has no equity in its capital structure and is financed entirely by debt. The equity reported on Big Sandy's balance sheet as "capital stock subscribed" of \$10,000 is offset by "other accounts receivable" of \$10,000 which does not conform to accounting procedures prescribed by the Uniform System of

Accounts, and indicates that no equity has been supplied by the owner. Therefore, the Commission has used debt service coverage ("DSC") in determining revenue requirements for Big Sandy.

Big Sandy's debt service is approximately \$14,782. Big Sandy's DSC on adjusted net operating income of \$24,471 is 1.65 X, which is greater than the 1.2 X that the Commission finds to be the fair, just, and reasonable coverage necessary for Big Sandy to pay its operating expenses and to meet the requirements of its lenders. Accordingly, the Commission has determined that no additional revenues are necessary.

SUMMARY

The Commission, after consideration of the record and being advised, is of the opinion and finds that:

1) The rates proposed by Big Sandy will provide revenues in excess of those found to be fair, just, and reasonable and should be denied upon application of KRS 278.030.

2) The current rates charged by Big Sandy as ordered in its previous rate case, Case No. 8014, are fair, just, and reasonable in that they produce annual revenues sufficient to meet operating expenses and debt service requirements and further, provide a reasonable surplus.

3) The provision of water service to customers in violation of Big Sandy's tariffed rates and of KRS 278.160 and 278.170 should immediately be ceased.

IT IS THEREFORE ORDERED that the rates proposed by Big Sandy will provide revenues in excess of those found to be fair, just, and reasonable and are hereby denied upon application of KRS 278.030.


IT IS FURTHER ORDERED that the provision of water service in violation of Big Sandy's tariffed rates and in violation of KRS 278.160 and 278.170 shall be ceased immediately.

IT IS FURTHER ORDERED that Big Sandy shall file copies of its billings, showing meter readings, usage, amounts billed, and any adjustments after each billing period, for 3 months after the date of this Order.

Done at Frankfort, Kentucky, this 21st day of December, 1982.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary